In the Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-706

ADOLPH COORS COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner challenges the decision below which held that it was not entitled to a current deduction for its indirect or overhead construction costs.

1. Petitioner produces and sells beer. It uses its own employees and equipment to erect buildings and other improvements and additions to its plant and facilities. During 1965 and 1966, petitioner respectively employed 398 and 580 persons engaged in construction. However, for accounting and tax purposes, petitioner has never separately identified its construction department. It employs a system of accounting which results in the current deduction rather than capitalization of all indirect or overhead costs of the construction activities (Pet. App. E 116a).

In a prior Tax Court proceeding dealing with petitioner's tax liability for 1962 through 1964, the Commissioner

raised several issues, including the deductibility of petitioner's construction costs. Following a trial of all issues, the Commissioner abandoned his challenge to petitioner's deduction of its construction costs for the prior years then in issue. However, the Commissioner expressly stated in his brief in the Tax Court (Commissioner's Brief, Docket Nos. 3179-66, 3180-66, 3181-66, pp. 3-3a) that he was not conceding the correctness of petitioner's accounting treatment of the construction costs. See Pet. App. E 117a. Accordingly, the Tax Court noted in its opinion in that prior case that "[t]he Commissioner in his brief abandons the disallowances of deductions made in the deficiency notice * * * representing corporation costs of construction overhead and maintenance and costs of engineering department overhead" (Pet. App. E 117a).

In this case, which involves the years 1965 and 1966, the Commissioner again disallowed various deductions for costs of construction overhead. On the merits, the Tax Court upheld the Commissioner's determination that such costs must be capitalized and were nondeductible. In so holding, the Tax Court rejected petitioner's claim that the capitalization issue was barred by collateral estoppel (Pet. App. D 44a-114a). The court of appeals affirmed (Pet. App. E 115a-121a).

2. The court of appeals properly held that the prior Tax Court decision did not constitute an adjudication of the merits of the accounting treatment issue. In that earlier case, the Commissioner merely withdrew the issue from consideration of the Tax Court. Accordingly, the Tax Court made no findings regarding the capitalization matter and did not address itself in any manner to a resolution of the legal issue.

Petitioner's position is that the issue was "litigated" in the prior case because evidence was adduced at trial, and because the Tax Court decision determined tax liability without capitalizing the costs in question. The

central inquiry, however, is not whether there has been a merely formal determination of liability in an earlier proceeding, but whether there has been an adjudication of a controverted issue submitted under adversary circumstances. Indeed, this Court has rejected the application of collateral estoppel even where the earlier determination *may* have been on the merits, in the absence of an affirmative showing that it was in fact based on the merits. *United States* v. *International Building Co.*, 345 U.S. 502, 506.[1] Here, of course, it is undisputed that the merits of the capitalization issue were not adjudicated in the case involving the earlier tax years.

3. This Court has narrowly limited the role of collateral estoppel in tax cases, for reasons amply illustrated by this case. Petitioner's position, if adopted, "would serve an unjust cause: it would become a device by which a decision not shown to be on the merits would forever foreclose inquiry into the merits." *United States* v. *International Building Co., supra,* 345 U.S. at 506. Moreover, on the merits *Commissioner* v. *Idaho Power Co.*, 418 U.S. 1, holding that the costs of equipment used by the taxpayer to build its own facilities must be capitalized as part of the cost of the capital improvements, would foreclose petitioner's claim to a deduction.[2]

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[1]Accord: *Trapp* v. *United States,* 177 F.2d 1(C.A. 10), certiorari denied, 339 U.S. 913 (earlier decision based on agreement of the parties, and deficiency calculated according to the contentions of the taxpayer); *Hartford-Empire Co.* v. *Commissioner,* 137 F.2d 540, 542 (C.A. 2) (estoppel not applicable "to matters not actually litigated"); *Licavoli* v. *Nixon,* 312 F.2d 200, 202 (C.A. 6) (estoppel denied where prior decision was based on "a procedural technicality"); 1B Moore's *Federal Practice,* para. 0.443[3] (2d ed., 1974).

[2]In *Idaho Power Co.* the Court cited the Tax Court's decision in this case with approval. See 418 U.S. at 14.

4. There is an additional ground, which the court of appeals did not find necessary to discuss, which renders collateral estoppel inapplicable here.

The Court's decision in *Commissioner* v. *Idaho Power Co., supra,* represents an intervening change in the "legal atmosphere" which would vitiate the force of collateral estoppel. See *Commissioner* v. *Sunnen, supra,* 333 U.S. at 600. Since *Idaho Power* represented "a modification or growth in legal principles" applicable to the issue, it nullified any potential or purported collateral estoppel effect of the earlier Tax Court decision. *Commissioner* v. *Sunnen, supra,* 333 U.S. at 599-600.

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

ROBERT H. BORK,
Solicitor General.

JANUARY 1976.